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THE VIEW
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A recipe for market bulls

Market fundamentals look unchanged, valuations are not stretched, and there is lots of money about – which all point to a bullish outlook for 2015

In October 2011, I wrote an article that choked out the words, “I am bullish”.

Three years later I am still bullish on shares. I know that the S&P has leapt 68 per cent since then. I know that Shanghai is up 41 per cent (mostly since November). The Hang Seng Index has given us a charitable 32 per cent in that time; Europe nothing.

These performances reflect the divergences in the global economy. US economic fortunes have soared, Europe’s have not, and China’s have declined.

This may say a great deal about my uncanny powers of forecasting – or perhaps not.

Markets were then extremely cheap in share price divided by company earnings terms. We had just experienced a big fall of 25 per cent in Hong Kong – following a rise of 100 per cent from the global financial crisis.

Economic growth was weak around the world but there were green shoots of recovery. It was a reasonably safe call.

To debunk my bullishness today, one must conjure up the spectre of “unknown unknowns” – unusual events that could overturn the status quo.

The major unknown is whether the stellar US economic performance could be damaged by weakness in the rest of the world. The US has done well enough without any outside help but obviously a major hitherto unknown event elsewhere in the world could tip the balance.

On the other hand the US Federal Reserve is likely to keep interest rates at the too low level of 0.25 per cent, for too long. The last time US growth was at 3 per cent per annum and unemployment was 5.6 per cent, interest rates were at 4.75 per cent!

We hear the cry, “but it’s the wrong kind of growth!” Three per cent rights a lot of wrongs and it seems more likely that 2015 will see other economies sparking into life rather than the wrong kind of growth fade.

Record low interest rates, plus record low inflation, collapsing energy bills, a high dollar reducing costs, and cheap labour merely demonstrates that the US is open for business.

Elsewhere economic policies that haven’t worked are being changed. The Europeans will this year panic into buying government bonds to reflate the economy. Surely good news for equities – if they can execute.

If this doesn’t work, there is plenty more going right. In 2011, the euro was at US\$1.40, it is now US\$1.18.

That makes BMW’s vehicles or Heidelberger’s printers some 16 per cent cheaper to a dollar buyer. It seems that the Germans at least are becoming more comfortable with weaker nations being ejected from the euro – if that happens, bet on a stock market surge.

The 50 per cent plummet in the oil price needs to be seen as a relief not a worry. Some estimates



The United States economy is open for business again.



The weakness of [Hong Kong] last year leaves room for a double-digit return this year

have it adding as much as a third to global GDP.

For instance, fuel comprises 38 per cent of Cathay Pacific’s costs; which is reflected in a share price jump of 20 per cent. Even if there were a “dead cat bounce” of 30 per cent tomorrow, oil would be at US\$60, down from US\$110 last summer.

For the markets to have a major, unrecoverable crash this year, we must first be in a bubble – a time of excessive stockmarket exuberance.

Yet the US is valued just 4 per cent above its long-term price-earnings average. Europe is just 3

per cent; but earnings are depressed, and should recover faster. This is not bubble territory.

The markets will be rightly concerned about interest rates going up in the US this year – but this has been flagged more than Occupy Central in Legco, and it seems unlikely that a miserable half point rise would give rise to an unrecoverable crash.

For investors, it may provide a buying opportunity, among others.

The timing seems right for a market rotation this year. The US already reflects its good fundamentals, so we might see only a single digit rise in 2015.

However, the stimuli mentioned above could drive double-digit returns from Europe, with only a mild further rise in the US dollar to dampen returns for Hong Kong investors. China and India should also benefit from economic reform, lower oil and higher exports.

In Hong Kong we bounce around like a cork on the sea, affected by global factors largely outside our control, but the relative weakness of the market last year leaves room for a double-digit return this year.

The crash will come – have no fear. But for this year, market fundamentals look unchanged, valuations are not stretched, and there is lots of money about. Barring any unknown unknowns, this is just the environment to spice up the market’s animal spirits. Which is why I am bullish.

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